Amendment No. 1 thereto prior to the thirtieth day after the date of publication of notice thereof in the **Federal Register**. The Commission notes that the Exchange's proposal, as amended, is similar to the NYSE and Nasdaq's proposals requiring shareholder approval of equity compensation plans. Both the NYSE and Nasdaq's proposals were published for comment in the **Federal Register** and recently approved by the Commission.[32] The Commission believes that it already considered and addressed the issues that may be raised by the Exchange's proposal in its approval of the NYSE and Nasdaq's proposals.[33]

The Commission believes that accelerated approval of the Exchange's proposal, as amended, is essential to allow for immediate harmonization of, and consistency in, the shareholder approval requirements for equity compensation plans among the markets. This will prevent issuers from making listing decisions based on differences in self-regulatory organization shareholder approval requirements and should provide equal investor protection to shareholders on the dilutive effects of plans irrespective of where the security trades. The Commission further believes that making the Exchange's new shareholder approval rules effective upon Commission approval will immediately impose the same requirements on the Exchange's issuers as those imposed upon NYSE, Nasdaq, and Amex issuers. Based on the above, the Commission finds good cause, consistent with Sections 6(b)(5) and 19(b)(2) of the Act,[34] to approve the Exchange's proposal and Amendment No. 1 thereto on an accelerated basis.

VI. Conclusion

It is therefore ordered, pursuant to Section 19(b)(2) of the Act,[35] that the proposed rule change (SR–CHX–2003–31) and Amendment No. 1 thereto are hereby approved on an accelerated basis.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.[36]

Jill M. Peterson,

Assistant Secretary.

[FR Doc. 03–28072 Filed 11–6–03; 8:45 am]

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–48738; File No. SR–CSE–2003–11]

Self-Regulatory Organizations; Notice of Filing and Order Granting Accelerated Approval to a Proposed Rule Change and Amendment No. 1 Thereto by the Cincinnati Stock Exchange Relating to Shareholder Approval of Equity Compensation Plans

October 31, 2003.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act''),[1] and Rule 19b–4 thereunder,[2] notice is hereby given that on October 1, 2003, the Cincinnati Stock Exchange (''CSE'' or ''Exchange'') filed with the Securities and Exchange Commission (''SEC'' or ''Commission'') the proposed rule change as described in Items I and II below, which Items have been prepared by the Exchange. On October 29, 2003, the Exchange filed Amendment No. 1 to the proposed rule change.[3] The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons and is approving the proposal and Amendment No. 1 thereto on an accelerated basis.

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The Exchange is proposing to implement changes to its listing standards to adopt requirements related to shareholder approval of equity compensation plans and to amend its rules related to the voting of proxies. The Exchange represents that this proposed rule change is part of an ongoing review of the Exchange's listing standards aimed at helping to restore investor confidence by strengthening corporate governance practices.

Below is the text of the proposed rule change. Proposed new language is *italicized*; proposed deleted language is [bracketed].

* * * * *

Rule 13.3 Proxies

(a)–(c) No change to text.

(d) Notwithstanding the provisions of this Rule 13.3, a member may not give a proxy to vote without instructions from beneficial owners when the matter to be voted upon authorizes the implementation of any equity compensation plan, or any material revision to the terms of any existing equity compensation plan (whether or not stockholder approval of such plan is required pursuant to Rule 13.6). This provision will be effective for any meeting of shareholders that occurs on or after the 90th day following the effective date of this provision.

* * * * *

Rule 13.6 Shareholder Approval of Equity Compensation Plans

Equity compensation plans can help align shareholder and management interests, and equity-based awards are often very important components of employee compensation. To provide checks and balances on the potential dilution resulting from the process of earmarking shares to be used for equity-based awards, the Exchange requires that all equity compensation plans, and any material revisions to the terms of such plans, be subject to shareholder approval, with limited exemptions identified in this rule.

(a) Definition of Equity Compensation Plan. An ''equity compensation plan'' is a plan or other arrangement that provides for the delivery of equity securities (either newly issued or treasury shares) of the listed company to any employee, director or other service provider as compensation for services. A compensatory grant of options or other equity securities that is not made under a plan is considered an ''equity compensation plan'' for purposes of these rules.

(b) Exceptions to Equity Compensation Plan Definition. The following are not equity compensation plans, even if the brokerage and other costs of the plan are paid for by the listed company:

(1) Plans that are made available to shareholders generally, such as a typical dividend reinvestment plan;

(2) Plans that merely allow employees, directors or other service

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[32] *See* Securities Exchange Act Release No. 46620 (October 8, 2002), 67 FR 63486 (notice of the NYSE's proposal). The Commission also published a correction to the notice of the NYSE's proposal. *See* Securities Exchange Act Release No. 44620A (October 21, 2002), 67 FR 65617 (October 25, 2002). *See* Securities Exchange Act Release No. 46649 (October 11, 2002), 67 FR 64173 (notice of Nasdaq's proposal). *See supra* note 4; *see also supra* note 19.

[33] Some of the substantive provisions ultimately adopted by the NYSE and Nasdaq, and now being proposed for adoption by the Exchange, were in response to these comments. The comments on the NYSE and Nasdaq proposals were also discussed in detail in the Commission's approval order of the NYSE and Nasdaq proposals. *See supra* note 4; *see also supra* note 19.

[34] 15 U.S.C. 78f(b)(5) and 78s(b)(2).

[35] 15 U.S.C. 78s(b)(2).

[36] 17 CFR 200.30–3(a)(12).

[1] 15 U.S.C. 78s(b)(1).

[2] 17 CFR 240.19b–4.

[3] *See* letter from Jennifer M. Lamie, Assistant General Counsel and Secretary, CSE, to Sapna C. Patel, Special Counsel, Division of Market Regulation, Commission, dated October 29, 2003 (''Amendment No. 1''). In Amendment No. 1, the Exchange made a technical correction to its proposed rule language to fix two typographical errors in proposed CSE Rule 13.6(e)(2). Because this is a technical amendment, it is not subject to notice and comment.

providers to elect to buy shares on the open market or from the listed company for their current fair market value, regardless of whether: (i) The shares are delivered immediately or on a deferred basis; or (ii) the payments for the shares are made directly or by giving up compensation that is otherwise due (for example, through payroll deductions).

(c) Material Revisions. A ''material revision'' of an equity compensation plan includes, but is not limited to, the following:

(1) A material increase in the number of shares available under the plan, other than an increase solely to reflect a reorganization, stock split, merger, spinoff or similar transaction.

(i) If a plan contains a formula for automatic increases in the number of shares available (sometimes referred to as an ''evergreen formula'') or for automatic grants pursuant to a formula, each such increase or grant will be considered a revision requiring shareholder approval unless the plan has a term of not more than ten years. Regardless of the term, this type of plan is referred to below as a ''formula plan.'' Examples of automatic grants pursuant to a formula are: (A) annual grants to directors of restricted stock having a certain dollar value, and (B) ''Matching contributions,'' whereby stock is credited to a participant's account based upon the amount of compensation the participant elects to defer.

(ii) If a plan contains no limit on the number of shares available and it is not a formula plan, then each grant under the plan will require separate shareholder approval regardless of whether the plan has a term of not more than ten years. This type of plan is referred to below as a ''discretionary plan.'' A requirement that grants be made out of treasury shares or repurchased shares will not, in itself, be considered a limit or pre-established formula so as to prevent a plan from being considered a discretionary plan.

(2) An expansion of the types of awards available under the plan.

(3) A material expansion of the class of employees, directors or other service providers eligible to participate in the plan.

(4) A material extension of the term of the plan.

(5) A material change to the method of determining the strike price of options under the plan.

(i) A change in the method of determining ''fair market value'' from the closing price on the date of the grant to the average of the high and low price on the date of grant is an example of a change that the Exchange would not review as material.

(6) The deletion or limitation of any provision prohibiting repricing of options. An amendment will not be considered a ''material revision'' if it curtails rather than expands the scope of the plan in question.

(d) Repricings. A plan that does not contain a provision that specifically permits repricing of options will be considered for purposes of this listing standard as prohibiting repricing. Accordingly, any actual repricing of options will be considered a material revision of a plan even if the plan itself is not revised. This consideration will not apply to a repricing through an exchange offer that commenced before the date this listing standard became effective. ''Repricing'' means any of the following or any other action that has the same effect:

(1) Lowering the strike price of an option after it is granted.

(2) Any other action that is treated as a repricing under generally accepted accounting principles.

(3) Canceling an option at a time when its strike price exceeds the fair market value of the underlying stock, in exchange for another option, restricted stock, or other equity, unless the cancellation and exchange occurs in connection with a merger, acquisition, spin-off or other similar corporate transaction.

(e) Exemptions. The listing standard does not require shareholder approval of employment inducement awards; certain grants, plans and amendments in the context of mergers and acquisitions; and certain specific types of plans, all described below. However, these exempt grants, plans and amendments may be made only with the approval of the company's independent compensation committee or the approval of a majority of the company's independent directors. Companies must also notify the Exchange in writing when they use one of these exemptions.

(1) Employment Inducement Awards. An employment inducement award is a grant of options or other equity-based compensation as a material inducement to a person or persons being hired by the listed company or any of its subsidiaries, or being rehired following a bona fide period of interruption of employment. Inducement awards include grants to new employees in connection with a merger or acquisition. Promptly following a grant of any inducement award in reliance on this exemption, the listed company must disclose in a press release the material terms of the award, including the recipient(s) of the award and the number of shares involved.

(2) Mergers and Acquisitions. Two exemptions apply in the context of corporate acquisitions and mergers. First, shareholder approval will not be required to convert, replace or adjust outstanding options or other equity compensation awards to reflect the transaction. Second, shares available under certain plans acquired in corporate acquisitions and mergers may be used for certain post-transaction grants without further shareholder approval. This exemption applies to situations where a party that is not a listed company following the transaction has shares available for grant under pre-existing plans that were previously approved by shareholders. A plan adopted in contemplation of the merger or acquisition transaction would not be considered ''pre-existing'' for purposes of this exemption. Shares available under such a pre-existing plan may be used for post-transaction grants of options and other awards with respect to equity of the entity that is the listed company after the transaction, either under the pre-existing plan or another plan, without further shareholder approval, so long as:

(i) The number of shares available for grants is appropriately adjusted to reflect the transaction;

(ii) The time during which those shares are available is not extended beyond the period when they would have been available under the pre-existing plan, absent the transaction; and

(iii) The options and other awards are not granted to individuals who were employed, immediately before the transaction, by the post-transaction listed company or entities that were its subsidiaries immediately before the transaction.

Any shares reserved for listing in connection with a transaction pursuant to either of these exemptions would be counted by the Exchange in determining whether the transaction involved the issuance of 20% or more of the company's outstanding common stock, and thus require shareholder approval. These merger-related exemptions will not result in any increase in the aggregate potential dilution of the combined enterprise. Further, mergers or acquisitions are not routine occurrences and are not likely to be abused. Therefore, the Exchange considers both of these exemptions to be consistent with the fundamental policy involved in this standard.

(3) Qualified Plans, Section 423 Plans and Parallel Excess Plans.

(i) The following types of plans, and material revisions thereto, are exempt from the shareholder approval requirement: (A) Plans intended to meet the requirements of Section 401(a) of the Internal Revenue Code (e.g., ESOPs); (B) plans intended to meet the requirements of Section 423 of the Internal Revenue Code; and (C) ''parallel excess plans'' as defined below.

(ii) Section 401(a) plans and Section 423 plans are already regulated under the Internal Revenue Code and Treasury regulations. Section 423 plans, which are stock purchase plans under which an employee can purchase no more than $25,000 worth of stock per year at a plan-specified discount capped at 15% are also required by the Internal Revenue Code to receive shareholder approval. While Section 401(a) plans and parallel plans are not required to be approved by shareholders, U.S. GAAP requires that the shares issued under these plans be ''expensed'' (i.e., treated as a compensation expense on the income statement) by the company issuing the shares. An equity compensation plan that provides non-U.S. employees with substantially the same benefits as a comparable Section 401(a) plan, Section 423 plan or parallel excess plan that the listed company provides to its U.S. employees, but for features necessary to comply with applicable foreign tax law, are also exempt from shareholder approval under this section.

(iii) The term ''parallel excess plan'' means a plan that is a ''pension plan'' within the meaning of the Employee Retirement Income Security Act (''ERISA'') that is designed to work in parallel with a plan intended to be qualified under Internal Revenue Code Section 401(a) to provide benefits that exceed the limits set forth in Internal Revenue Code Section 402(g)(the section that limits an employee's annual pre-tax contributions to a 401(k) plan), Internal Revenue Code Section 401(a)(17)(the section that limits the amount of an employee's compensation that can be taken into account for plan purposes) and/or Internal Revenue Code Section 415 (the section that limits the contributions and benefits under qualified plans) and/or any successor or similar limitations that may hereafter be enacted. A plan will not be considered a parallel excess plan unless: (A) it covers all or substantially all employees of an employer who are participants in the related qualified plan whose annual compensation is in excess of the limit of Internal Revenue Code Section 401(a)(17)(or any successor or similar limits that may hereafter be enacted); (B) its terms are substantially the same as the qualified plan that it parallels except for the elimination of the limits described in the proceeding sentence and the limitation described in clause (C); and (C) no participant receives employer equity contributions under the plan in excess of 25% of the participant's cash compensation.

(f) Transition Rules. Except as provided below, a plan that was adopted before the date the Commission order approving this listing standard will not be subject to shareholder approval under this Rule 13.6 unless and until it is materially revised.

(1) In the case of a discretionary plan, as defined in ''Material Revisions'' above, whether or not previously approved by shareholders, additional grants may be made after the effective date of this Rule 13.6 without further shareholder approval only for a limited transaction period, defined below, and then only in a manner consistent with past practice. In applying this rule, if a plan can be separated into a discretionary plan portion and a portion that is not discretionary, the non-discretionary portion of the plan can continue to be used separately, under the appropriate transition rule. For example, if a shareholder-approved plan permits both grants pursuant to a provision that makes available a specific number of shares, and grants pursuant to provision authorizing the use of treasury shares without regard to the specific share limit, the former provision (but not the latter) may continue to be used after the transition period, under the general rule above.

(2) In the case of a formula plan, as defined in ''Material Revisions'' above, that either (i) has not previously been approved by shareholders or (ii) does not have a term of ten years or less, additional grants may be made after the effective date of this Rule 13.6 without further shareholder approval only for a limited transition period, defined below.

(3) The limited transition period described in subparagraphs (f)(1) and (f)(2) above will end upon the first to occur of: (i) The listed company's next annual meeting at which directors are elected that occurs more than 180 days after the effective date of this listing standard; (ii) the first anniversary of the effective date this Rule 13.6; and (iii) the expiration of the plan.

(4) A shareholder-approved formula plan may continue to be used after the end of this transition period if it is amended to provide for a term of ten years or less from the date of its original adoption or, if later, the date of its most recent shareholder approval. Such an amendment may be made before or after the effective date of this Rule 13.6, and would not itself be considered a ''material revision'' requiring shareholder approval. In addition, a formula plan may continue to be used, without shareholder approval, if the grants after the effective date of this Rule 13.6 are made only from the shares available immediately before the effective date (i.e., based on formulaic increases that occurred prior to such effective date).

(g) Broker Voting. For member proxy requirements with respect to the implementation of any equity compensation plan, or any material revisions to the terms of any existing equity compensation plan, refer to Rule 13.3.

* * * * *

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the Exchange included statements concerning the purpose of, and basis for, the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item III below. The Exchange has prepared summaries, set forth in Sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

In conjunction with a review of its corporate listing standards with the goal of enhancing accountability, integrity and transparency of listed companies, the Exchange is proposing to adopt listing standards related to shareholder approval of equity compensation plans and to amend its rules related to the voting of proxies.[4]

[4] The Commission notes that the Exchange is proposing to adopt listing standards relating to shareholder approval of equity compensation plans that are similar to those that the Commission recently approved for the New York Stock Exchange, Inc. (''NYSE'') and the National Association of Securities Dealers, Inc. (''NASD''), through its subsidiary, The Nasdaq Stock Market, Inc. (''Nasdaq''). *See* Securities Exchange Act Release No. 48108 (June 30, 2003), 68 FR 39995 (July 3, 2003) (order approving File Nos. SR–NYSE–2002–46 and SR–NASD–2002–140). *See also* Securities Exchange Act Release No. 48627 (October 14, 2003), 68 FR 60426 (October 22, 2003) (notice of filing and order granting accelerated approval to File No. SR–NASD–2003–130, incorporating amendments to the NASD's recently approved shareholder approval rules for equity compensation plans applicable to Nasdaq quoted securities). The Commission also published a correction to the

The Exchange is proposing to adopt new CSE Rule 13.6, which would require shareholder approval of all equity-compensation plans and material revisions to such plans, subject to limited exemptions. Under the Exchange's proposal, an equity compensation plan is defined as a plan or other arrangement that provides for the delivery of equity securities (either newly issued or treasury shares) of the listed company to any employee, director or other service provider as compensation for services, including a compensatory grant of options or other equity securities that is not made under a plan. The Exchange is also proposing to provide clarification on certain plans that would not be considered equity compensation plans under this definition, such as plans that do not provide for delivery of equity securities of the issuer (*e.g.,* plans that pay in cash) and deferred compensation plans under which employees pay full current market value for deferred shares.

In addition, the proposal provides for certain types of grants that are exempted from shareholder approval. These limited exemptions include: (1) Inducement awards to person's first becoming an employee of an issuer or any of its subsidiaries, to rehires following a *bona fide* period of employment interruption, and for grants to new employees in connection with a merger or acquisition;[5] (2) mergers and acquisitions, when conversions, replacements or adjustments of outstanding options or other equity compensation awards are necessary to reflect the transaction, and when shares available under certain plans acquired in corporate acquisitions and mergers may be used for certain post-transaction grants without further shareholder approval; and (3) plans intended to meet the requirements of Section 401(a) of the Internal Revenue Code[6] (*e.g.,* ESOPs), plans intended to meet the requirements of Section 423 of the Internal Revenue Code,[7] and parallel excess plans that meet certain conditions. The Exchange also proposes that, in circumstances in which equity compensation plans and amendments to plans are not subject to shareholder approval, the plans and amendments still must be subject to the approval of the company's independent compensation committee or a majority of the company's independent directors. In addition, the Exchange proposes that an issuer must notify the Exchange in writing when it uses any of the exemptions from the shareholder approval requirements.

The Exchange is also proposing to provide a non-exclusive list of ''material revisions'' to a plan that would require shareholder approval. Within this list of revisions, the Exchange proposes to define the concepts of ''evergreen plans'' (*i.e.*, plans that contain a formula for automatic increases in the shares available), ''formula plans'' (*i.e.*, plans that provide for automatic grants pursuant to a formula), and ''discretionary plans'' (*i.e.*, plans that contain no limit on the number of shares available and plans that are not formula plans). The Exchange proposes that each grant under a discretionary plan require shareholder approval regardless of whether the plan has a term of not more than 10 years.

Shareholder approval will be required for plans adopted before the effective date of these proposed amendments that have not been approved by shareholders and have neither an evergreen formula nor a specific number of shares available under the plan. The Exchange is proposing to provide transition rules to clarify when shareholder approval will be required for these pre-existing plans. In addition, during the period prior to the approval, pre-existing plans may be utilized, but only in a manner consistent with past practice. The transition rules provide that an evergreen plan that was approved by shareholders but does not have a ten-year term must be: (1) Approved by shareholders before any shares that become available as a result of a formulaic increase are utilized, or (2) amended to include a term of no more than ten years from the date the plan was adopted or last approved by shareholders. If the plan were amended to include such term, shareholder approval would not be required. No action would be required, however, if a plan were frozen at the level of shares available at the time the rule becomes effective. The transition rules also provide that repricings that have commenced prior to the effectiveness of the proposal (*i.e.,* exchange offers to optionees) will not be subject to shareholder approval (assuming that such repricing would not require shareholder approval under other Exchange By-Laws or Rules).

Finally, the Exchange is also proposing to amend CSE Rule 13.3 to prohibit members from voting on equity compensation plans unless the beneficial owner of the shares has given voting instructions. The Exchange proposes a transition period that will make these provisions of CBOE Rule 13.3 applicable only to shareholder meetings that occur on or after the 90th day following the date of the Commission order approving the rule.

2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with Section 6 of the Act,[8] in general, and furthers the objectives of Section 6(b)(5) of the Act,[9] in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest.

B. Self-Regulatory Organization's Statement on Burden on Competition

The Exchange does not believe that the proposed rule change will impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others

Written comments on the proposed rule change were neither solicited nor received.

III. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549–0609. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be

notice of File No. SR–NASD–2003–130. *See* Securities Exchange Act Release No. 48627A (October 22, 2003), 68 FR 61532 (October 28, 2003). The Commission notes that these additional amendments by Nasdaq make the NYSE and Nasdaq proposals more consistent and uniform. *See also infra* note (regarding the Commission's recent approval of a similar proposal by the American Stock Exchange LLC (''Amex'')).

[5] The Exchange is also proposing to include a requirement that listed companies provide prompt public disclosure following the grant of any inducement award in reliance on the exemption.

[6] 26 U.S.C. 401(a).

[7] 26 U.S.C. 423.

[8] 15 U.S.C. 78f(b).

[9] 15 U.S.C. 78f(b)(5).

available for inspection and copying at the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of the Exchange. All submissions should refer to File No. SR-CSE–2003–11 and should be submitted by November 28, 2003.

IV. Commission's Findings and Order Granting Accelerated Approval to the Proposed Rule Change

After careful review, the Commission finds that the Exchange's proposal is consistent with the Act and the rules and regulations promulgated thereunder applicable to a national securities exchange and, in particular, with the requirements of Section 6(b) of the Act.[10] Specifically, the Commission finds that approval of the Exchange's proposal is consistent with Section 6(b)(5) of the Act[11] in that it is designed to, among other things, facilitate transactions in securities; to prevent fraudulent and manipulative acts and practices; to promote just and equitable principles of trade; to remove impediments to and perfect the mechanism of a free and open market and a national market system; and, in general, to protect investors and the public interest; and does not permit unfair discrimination among issuers.

The Commission has long encouraged exchanges to adopt and strengthen their corporate governance listing standards in order to, among other things, restore investor confidence in the national marketplace. The Commission believes that the Exchange's proposal, which requires shareholder approval of equity compensation plans and which follows the Commission's approval of similar proposals by the NYSE, Nasdaq, and Amex[12] is the first step under this directive because it should have the effect of safeguarding the interests of shareholders, while placing certain restrictions on Exchange-listed companies.

In addition, the Commission notes that the Exchange's proposal is similar and almost identical to proposals by NYSE and Nasdaq requiring shareholder approval of equity compensation plans that have previously been approved by the Commission.[13] The Commission believes that it has already considered and addressed the issues that may be raised by the Exchange's proposal when it approved these proposals. The Commission notes that approval of the Exchange's proposal will conform the Exchange's shareholder approval requirements for equity compensation plans with those of the NYSE and Nasdaq, and will immediately impose the same requirements on the Exchange's issuers as those imposed upon NYSE, Nasdaq, and Amex issuers. The adoption of these standards by the Exchange is an important step to ensure that issuers will not be able to avoid shareholder approval requirements for equity compensation plans based on their listed marketplace.

A. Exemption From Shareholder Approval for Inducement Grants

The Commission believes that the requirement that the issuance of all inducement grants be subject to review by either the issuer's independent compensation committee or a majority of the board's independent directors, under the Exchange's proposal, should prevent abuse of this exemption from shareholder approval. In addition, the Exchange proposes to limit its exemption for inducement grants to new employees or to previous employees being rehired after a bona fide period of interruption of employment, and to new employees in connection with an acquisition or merger. The Commission believes that these limitations should help to prevent the inducement exemption from being used inappropriately.

The Commission notes that the Exchange is proposing to include a requirement, similar to the requirement under the NYSE and Nasdaq's recently approved shareholder approval rules, that, promptly following the grant of any inducement award, companies must disclose in a press release the material terms of the award, including the recipient(s) of the award and the number of shares involved.[14] The Commission notes that the Exchange is also proposing a requirement, similar to the requirements under the NYSE and Nasdaq's recently approved shareholder approval rules,[15] that an issuer must notify it in writing when it uses this exemption, and/or any other exemption, from its shareholder approval requirement. The Commission believes that these disclosure and notification requirements will provide transparency to investors and should reduce the potential for abuse of this exemption for inducement grants.

B. Exemption From Shareholder Approval for Mergers and Acquisitions

The Commission notes that the Exchange's exemption from shareholder approval for mergers and acquisitions contains safeguards that should prevent abuse in this area. First, only pre-existing plans that were previously approved by the acquired company's shareholders would be available to the listed company for post-transactional grants. In addition, shares under those previously approved plans could not be granted to individuals who were employed, immediately before the transaction, by the post-transaction listed company or its subsidiaries. The Commission also notes that, under the Exchange's proposal, any shares reserved for listing in connection with a merger or acquisition pursuant to this exemption would be counted by the Exchange in determining whether the transaction involved the issuance of 20% or more of the company's outstanding common stock, thereby requiring shareholder approval. Finally, the Commission notes that the Exchange proposes an additional requirement that an issuer must notify it in writing when it uses this exemption, and/or any other exemption, from its shareholder approval requirement. Based on the above, the Commission believes that the Exchange has provided measures to ensure that the exemption for mergers and acquisitions is only used in limited circumstances, which should help reduce the potential for dilution of shareholder interests.

C. Exemption From Shareholder Approval for Tax Qualified and Parallel Nonqualified Plans

The Commission believes that, given the extensive government regulation—the Internal Revenue Code and Treasury regulations—for tax qualified plans and the general limitations associated with parallel nonqualified plans, shareholders should not experience significant dilution as a result of this exemption. In addition, the Commission notes that the Exchange proposes to add

[10] 15 U.S.C. 78f(b). In approving the Exchange's proposal, the Commission has considered the proposed rule's impact on efficiency, competition and capital formation. 15 U.S.C. 78c(f).

[11] 15 U.S.C. 78f(b)(5).

[12] *See supra* note 4. The Commission notes that it has recently approved similar rules requiring shareholder approval of equity compensation plans for the Amex on an accelerated basis. The Amex's proposal is almost identical to, and based on, the NYSE and Nasdaq proposals. *See* Securities Exchange Act Release No. 48610 (October 9, 2003), 68 FR 59650 (October 16, 2003).

[13] *See supra* notes 4 and 12.

[14] This disclosure would, of course, be in addition to any information that is required to be disclosed in annual reports filed with the Commission. For example, Item 201(d) of Regulation S–K (17 CFR 229.201(d)) and Item 201(d) of Regulation S–B (17 CFR 228.201(d)) require issuers to present—in their annual reports on Form 10–K or Form 10–KSB—separate, tabular disclosure concerning equity compensation plans that have been approved by shareholders and equity compensation plans that have not been approved by shareholders.

[15] *See* Section 303A(8) of the NYSE's *Listed Company Manual* and NASD Rules 4310(c)(17)(A) and 4320(e)(15)(A).

a limitation under this exemption that a plan would not be considered a nonqualified parallel plan under its proposal if employees who are participants in such a plan receive employer contributions under the plan in excess of 25% of the participants' cash compensation. The Commission further notes that the Exchange proposes an additional requirement that an issuer must notify it in writing when it uses this exemption, and/or any other exemption, from its shareholder approval requirement. The Commission believes that, taken together, these limitations should reduce concerns regarding abuse of this exemption from the shareholder approval requirements.

In addition, the Commission notes that, similar to the exemptions in the NYSE and Nasdaq's recently approved shareholder approval rules, the Exchange proposes to adopt an exemption from the shareholder approval requirements for an equity compensation plan that provides non-U.S. employees with substantially the same benefits as a comparable Section 401(a) plan, Section 423 plan or parallel excess plan that the listed company provides to its U.S. employees, but for features necessary to comply with applicable foreign tax law. The Commission believes that this change will conform the Exchange's shareholder approval rule to that of the NYSE and Nasdaq and will provide greater clarity for issuers regarding tax qualified, non-discriminatory employee benefit plans and parallel nonqualified plans for their non-U.S. employees.

D. Material Revisions to Plans

The Commission notes that the Exchange proposes to provide a non-exclusive list, similar to lists found in the NYSE and Nasdaq's shareholder approval rules,[16] as to what constitutes a material revision to a plan. As noted above, material revisions to plans will require shareholder approval under Exchange rules. A material revision under the Exchange's proposal would include, but is not limited to: a material increase in the number of shares to be issued under the plan (other than to reflect a reorganization, stock split, merger, spinoff or similar transaction); an expansion of the type of awards available under the plan; a material expansion of the class of participants eligible to participate in the plan; a material extension of the term of the plan; a material change to limit or delete any provisions prohibiting repricing of options in a plan or for determining the strike or exercise price of options under a plan. The Exchange's proposal also describes what would constitute a material revision for plans containing a formula for automatic increases (such as evergreen plans) and automatic grants requiring shareholder approval.

The Commission believes that the Exchange's non-exclusive list of what would constitute a material revision to a plan provides companies with clarity and guidance for when certain amendments and revisions to plans would require shareholder approval. The Commission also believes that the Exchange's proposal to conform its non-exclusive list with the NYSE and Nasdaq's rules on material amendments/revisions should help to ensure that the concept of material amendments/revisions is consistent among the markets so that differences between the markets cannot be abused.

E. Repricing of Plans

The Commission notes that the Exchange's proposal provides that, if a plan explicitly contains a repricing provision, shareholder approval would be required to delete or limit the repricing provisions. The Commission further notes that the Exchange's proposal provides that, if a plan is silent on repricing, it will be considered as prohibiting repricing and shareholder approval would be required to permit repricing under the plan. The Exchange's proposal also clarifies that repricings that have commenced prior to the date of effectiveness of its proposal would not be subject to shareholder approval, provided that such repricing does not require shareholder approval under the Exchange's existing shareholder approval rules.

The Commission believes that the Exchange's proposal should benefit shareholders by ensuring that companies cannot do a repricing of options, which can have a dilutive effect on shares, without explicit shareholder approval of such provisions and their terms. The Commission also believes that the Exchange's approach to repricings is similar to the NYSE and Nasdaq's respective approaches to repricings, and should offer companies clarity and guidance as to when a change in a plan regarding the repricing of options would trigger a shareholder approval requirement.

F. Evergreen or Formula Plans and Plans Without a Formula or Limit on the Number of Shares Available

The Commission notes the Exchange's proposal provides guidance for the treatment of evergreen/formula plans. More specifically, under the Exchange's proposal, if a plan contains a formula for automatic increases in the shares available or for automatic grants pursuant to a formula, such plans cannot have a term in excess of ten years unless shareholder approval is obtained every ten years. In addition, under the Exchange's proposal, if a plan contains no limit on the number of shares available and is not a formula plan, then each grant under the plan will require separate shareholder approval. Furthermore, the Exchange's proposal provides that a requirement that grants be made out of treasury or repurchased shares will not alleviate the need for shareholder approval for additional grants.

The Commission believes that these provisions should help to ensure that certain terms of a plan cannot be drafted so broad as to avoid shareholder scrutiny and approval. The Commission also believes that the Exchange's proposed rules relating to the treatment of evergreen/formula plans and plans that do not contain a formula or place a limit on the number of shares available should provide more clarity and transparency to issuers as to when shareholder approval would be required for such plans. Finally, the Commission believes that the provision ensuring that treasury and repurchased shares cannot be used to avoid these additional shareholder approval requirements strengthens the proposal and ensures that companies cannot avoid compliance with the rule.

The Commission further notes that the Exchange has proposed a transition period for evergreen/formula plans and discretionary plans. The limited transition period would end on the first to occur of the following: (1) The listed company's next annual meeting at which directors are elected that occurs more than 180 days after the date of the effective date of the Exchange's proposal; (2) the first anniversary of the effective date of the Exchange's proposal; or (3) the expiration of the plan. The Commission believes that the Exchange's proposed transition period for evergreen/formula and discretionary plans should provide companies with additional clarity and guidance as to when shareholder approval would be required for such plans while in the transition period, and should provide companies with more time to comply with the Exchange's new shareholder approval requirements for evergreen/formula type plans. The Commission believes that this period is not so long as to permit abuse of the shareholder approval requirement, and at most, will last one year from the date of this Commission approval order.

[16] *See supra* note 4; *see also supra* note 12.

G. Miscellaneous Provisions

The Commission notes that the Exchange's proposal—similar to the NYSE and Nasdaq's recently approved shareholder approval rules [17]—incorporates the term ''equity compensation'' and proposes that plans that merely provide a convenient way to purchase shares in the open market or from the issuer at fair market price on equal terms to all security holders would not require shareholder approval. The Commission believes that the Exchange's proposal is consistent with the NYSE and Nasdaq's rules in this area and should provide greater clarity with respect to which plans would and would not require shareholder approval.

The Commission notes that the Exchange's proposal provides that pre-existing plans, which were adopted prior to the SEC's approval of the Exchange's proposal, would essentially be ''grandfathered'' and would not require shareholder approval unless the plans were materially amended. Under the Exchange's proposal, however, shareholder approval is required for each grant made pursuant to any pre-existing plans that were not approved by shareholders and that do not have an evergreen formula or a specific number of shares available under the plan. This is consistent with the NYSE, Nasdaq, and Amex shareholder approval rules on this matter. The Commission believes that this clarification should provide companies with guidance as to which plans would be subject to the Exchange's new shareholder approval requirements.

H. Elimination of Broker-Dealer Voting on Equity Compensation Plans

The Commission believes that the Exchange's proposed provision, CSE Rule 3.3(d), to preclude broker voting on equity compensation plans is consistent with the Act. The Commission notes that equity compensation plans have become an important issue for shareholders. Because of the potential for dilution from issuances under such plans, shareholders should be making the determination rather than brokers on their behalf. The Commission further notes that NASD rules do not provide for broker voting on any matters, and NYSE rules prohibit broker voting on equity compensation plans.[18] Therefore, the Exchange's proposed provision would be consistent with NASD and NYSE rules regarding broker voting on equity compensation plans. The Commission has considered the impact on smaller issuers, such as those listed on Nasdaq and the Amex, in response to the comments on this issue.[19] The Commission believes that the benefit of ensuring that the votes reflect the views of beneficial shareholders on equity compensation plans outweighs the potential difficulties in obtaining the vote.

The Commission also notes that the Exchange proposes to implement a transition period that would make the new rule eliminating broker voting on equity compensation plans applicable only to shareholder meetings that occur on or after the 90th day from the effective date of the Exchange's proposal.

I. Summary

Overall, the Commission believes that the Exchange's proposal is similar to the NYSE and Nasdaq's recently approved shareholder approval rules.[20] The Commission therefore believes that the Exchange's proposal should provide for more clear and uniform standards for shareholder approval of equity compensation plans. The Commission notes that, even with the availability of the proposed limited exemptions from shareholder approval under the Exchange's proposal, shareholder approval under the new standards would be required in more circumstances than under existing Exchange rules. The Commission further notes that the Exchange proposes to adopt a requirement that an issuer must notify it in writing when it uses one of the exemptions from the shareholder approval requirements. The Commission believes that such a requirement, coupled with the additional disclosure requirements for inducement grants, should reduce the potential for abuse of any of the exemptions.[21] In addition, the Exchange's proposed amendment to CSE Rule 13.3, which would preclude broker-dealers from voting on equity compensation plans without explicit instructions from the beneficial owner, is consistent with the standard under current NYSE and NASD rules.

The Commission believes that the Exchange's proposal, which is similar to the NYSE and Nasdaq's shareholder approval rules,[22] sets a consistent, minimum standard for shareholder approval of equity compensation plans. The Commission believes that the Exchange's proposal should help to ensure that companies will not make listing decisions simply to avoid shareholder approval requirements for equity compensation plans and should provide shareholders with greater protection from the potential dilutive effect of equity compensation plans. Based on the above, the Commission finds that the Exchange's proposal should help to protect investors, is in the public interest, and does not unfairly discriminate among issuers, consistent with Section 6(b)(5) of the Act.[23] The Commission therefore finds the Exchange's proposal to be consistent with the Act and the rules and regulations thereunder.

V. Accelerated Approval of the Exchange's Proposal and Amendment No. 1

The Commission finds good cause for approving the Exchange's proposal and Amendment No. 1 thereto prior to the thirtieth day after the date of publication of notice thereof in the **Federal Register**. The Exchange has requested accelerated approval of the proposed rule change so as to avoid a delay in the implementation of these listing standards designed to protect investors and the public interest, which standards the Exchange represents are substantially similar to standards recently approved by the Commission for the NYSE and Nasdaq. The Exhange therefore believes that the Exchange's adoption of the proposed listing standards presents no novel issues. The Commission notes that the Exchange's proposal is similar to the NYSE and Nasdaq's proposals requiring shareholder approval of equity compensation plans. Both the NYSE and Nasdaq's proposals were published for comment in the **Federal Register** and recently approved by the Commission.[24] The Commission believes that it already considered and addressed the issues that may be raised by the Exchange's proposal in its approval of the NYSE and Nasdaq's proposals.[25]

[17] *See supra* note 4; *see also supra* note 12.

[18] *See* NASD Rule 2260; NYSE Rule 452; and Section 402.08 of the NYSE's *Listed Company Manual.*

[19] *See supra* notes 4 and 18.

[20] *See supra* note 4; *see also supra* note 12.

[21] *See also supra* note 14 and accompanying text.

[22] *See supra* note 4; *see also supra* note 12.

[23] 15 U.S.C. 78f(b)(5).

[24] *See* Securities Exchange Act Release No. 46620 (October 8, 2002), 67 FR 63486 (notice of the NYSE's proposal). The Commission also published a correction to the notice of the NYSE's proposal. *See* Securities Exchange Act Release No. 44620A (October 21, 2002), 67 FR 65617 (October 25, 2002). *See* Securities Exchange Act Release No. 46649 (October 11, 2002), 67 FR 64173 (notice of Nasdaq's proposal). *See supra* note 4; *see also supra* note 12.

[25] Some of the substantive provisions ultimately adopted by the NYSE and Nasdaq, and now being proposed for adoption by the Exchange, were in response to these comments. The comments on the NYSE and Nasdaq proposals were also discussed in detail in the Commission's approval order of the NYSE and Nasdaq proposals. *See supra* note 4; *see also supra* note 12.

The Commission believes that accelerated approval of the Exchange's proposal is essential to allow for immediate harmonization of, and consistency in, the shareholder approval requirements for equity compensation plans among the markets. This will prevent issuers from making listing decisions based on differences in self-regulatory organization shareholder approval requirements and should provide equal investor protection to shareholders on the dilutive effects of plans irrespective of where the security trades. The Commission further believes that making the Exchange's new shareholder approval rules effective upon Commission approval will immediately impose the same requirements on the Exchange's issuers as those imposed upon NYSE, Nasdaq, and Amex issuers. Based on the above, the Commission finds good cause, consistent with Sections 6(b)(5) and 19(b)(2) of the Act,[26] to approve the Exchange's proposal and Amendment No. 1 thereto on an accelerated basis.

VI. Conclusion

It Is Therefore Ordered, pursuant to Section 19(b)(2) of the Act,[27] that the proposed rule change (SR–CSE–2003–11) and Amendment No. 1 thereto are hereby approved on an accelerated basis.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.[28]

Jill M. Peterson,

Assistant Secretary.

[FR Doc. 03–28074 Filed 10–30–03; 8:45 am]

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–48735; File No. SR–PCX–2003–50]

Self-Regulatory Organizations; Notice of Filing and Order Granting Accelerated Approval to a Proposed Rule Change by the Pacific Exchange, Inc. Relating to its Shareholder Approval Policy for Its Listed Companies Regarding Stock Option Plans and Other Equity Compensation Arrangements

October 31, 2003.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act''),[1] and Rule 19b–4 thereunder,[2] notice is hereby given that on September 22, 2003, the Pacific Exchange, Inc. (''PCX'' or ''Exchange''), through its wholly owned subsidiary PCX Equities, Inc. (''PCXE''), filed with the Securities and Exchange Commission (''SEC'' or ''Commission'') the proposed rule change as described in Items I and II below, which Items have been prepared by the Exchange. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons and is approving the proposal on an accelerated basis.

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The Exchange, through PCXE, is proposing to amend its Section 3, Corporate Governance and Disclosure Policies, and more specifically PCXE Rule 5.3(d), Shareholder Approval Policy, relating to stock option plans and other equity compensation arrangements. The Exchange, through PCXE, is also proposing to amend PCXE Rule 9.4, Proxies Voting, to prohibit the holder of an Equity Trading Permit (''ETP'') from voting on equity compensation plans unless the beneficial owner of the shares has given voting instructions. The Exchange believes that the proposed changes are aimed at helping to restore investor confidence by strengthening listed companies' corporate governance practices.

Below is the text of the proposed rule change.[3] Proposed new language is *italicized*; proposed deleted language is [bracketed].

* * * * *

PCX Equities, Inc.

Rule 5

Listings

Rules 5.1–5.2—No change.

Section 3. Corporate Governance and Disclosure Policies

Corporate Governance and Disclosure Policies

Rule 5.3—No Change.

Rule 5.3(a)–5.3(c)—No Change.

Shareholder Approval Policy

Rule 5.3(d) Shareholder Approval Policy

Each issuer shall require shareholder approval of a plan or arrangement *pursuant to* [under] subparagraph*s* (1) *through (7)* below or, prior to the issuance of designated securities under subparagraphs *(8)* [(2)] through *(11)* [(4)] below.[, when:]

(1) *Shareholder Approval. Except as provided for in this Rule 5.3(d) all equity-compensation plans, and any material revisions to the terms of such plans, must be approved by the shareholders of the listed company.* [A stock option or purchase plan is to be established or other arrangement made pursuant to which stock may be acquired by officers or directors, except for warrants or rights issued generally to security holders of the company or broadly based plans or arrangements including other employees (*e.g.*, ESOPs).

The Corporation will generally not require shareholder's approval as a condition to listing shares reserved for the exercise of options when:

(i) such options are issued to an individual, not previously employed by the company, as an inducement essential to the individual's entering into an employment contract with the company provided that the potential issuance of shares pursuant to such options does not exceed 5% of the company's outstanding common stock; or

(ii) the establishment of a plan or arrangement under which the amount of securities which may be issued does not exceed the lesser of 1% of the number of shares outstanding common stock, 1% of the voting power outstanding, or 25,000 shares and provided that all arrangements adopted without shareholder approval in any five-year period do not authorize, in the aggregate, the issuance of more than 10% of outstanding common stock or voting power outstanding. (For the purpose of calculating the percentage of stock issued in aggregate, stock to be issued pursuant to options which have expired and/or been cancelled shall not be included.)]

(2) Equity Compensation Plan Defined. An equity compensation plan is a plan or other arrangement that provides for the delivery of equity securities (either newly issued or treasury shares) of the listed company to any employee, director or other service provider as compensation for services. For purposes of this rule, a compensatory grant of options or other equity securities that is not made under

[26] 15 U.S.C. 78f(b)(5) and 78s(b)(2).

[27] 15 U.S.C. 78s(b)(2).

[28] 17 CFR 200.30–3(a)(12).

[1] 15 U.S.C. 78s(b)(1).

[2] 17 CFR 240.19b–4.

[3] Upon the Exchange's request, the Commission made a technical correction to the proposed rule text. Telephone conversation between Steven B. Matlin, Senior Counsel, Regulatory Policy, PCX, and Sapna C. Patel, Special Counsel, Division of Market Regulation, Commission, on October 17, 2003.